No. 15110.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

JOHN LUCAS HUDSON, SR., and PACIFIC-PALMDALE DEVELOPMENT COMPANY, a corporation,

Appellants.

vs.

WILLIAM A. WYLIE, as Trustee in Bankruptcy of the Estate of John Lucas Hudson, Sr., a bankrupt,

Appellee.

APPELLEE'S BRIEF.

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APPELLEE'S BRIEF.

Jurisdictional Statement.

Examination of the transcript of the record on appeal, the index thereof on pages I, II and III and the designation of record to be printed on appeal of the appellant dated April 23, 1956 and set forth on page 366 of the Transcript of Record on Appeal will disclose that neither the Designation of the Record to be Printed on Appeal nor the Transcript of the Record on Appeal contain any evidence as to the Petition in Bankruptcy, any Order of Adjudication, or any Order referring the matter to a Referee in Bankruptcy. It is therefore respectfully submitted that the Record on Appeal is devoid of evidence upon which this Court may base its jurisdiction, and the Court should rule that it does not have jurisdiction to hear this appeal based on the record before it.

Statement of the Case.

Late in 1952 or early in 1953 the bankrupt made an assignment for benefit of creditors and was unsuccessful in obtaining a release from his creditors [Tr. p. 205], and at the time of the contract with the Commodity Credit Corporation hereinafter referred to, the said assignment for benefit of creditors was still in force and effect [Tr. pp. 205, 206, 207].

In the summer of 1953 Mr. Merrill L. Granger, the bankrupt's attorney throughout this proceeding in all matters referred to herein, prepared a document which was executed by the bankrupt and his wife, the effect of which was to give the wife all of her earnings as her sole and separate property, the purpose of the said agreement being to enable the bankrupt to get started in business again without creditors of the bankrupt being able to attack his earnings. [Tr. pp. 232, 233 and Ex. "C" in the proceedings before the Referee]. At this time Mr. Merrill L. Granger, the attorney for the bankrupt, was familiar with the law relating to bankruptcies and had specialized at a prior date in assignments for benefit of creditors and creditors' rights law, [Tr. pp. 315 to 316], and at all times herein mentioned the said Merrill L. Granger had knowledge of the aforementioned assignment for benefit of creditors, and that the same was without a release of creditors. [Tr. pp. 316-319].

At all times herein mentioned the said Merrill L. Granger had no special knowledge or skill as regards the construction or erection of grain bins [Tr. p. 326], and the bankrupt had personal knowledge and skill regarding the submission of bids for grain bins and the construction thereof. [Tr. pp. 72-74]. On numerous

occasions during the period between the summer of 1954 and the date of bankruptcy, the bankrupt was advised by Mr. Granger that if he accumulated substantial earnings without a release from his creditors the accumulation would be subject to the creditors' demands [Tr. p. 267]; that he should not commit his services [Tr. p. 197], and that he should not be an officer of a corporation [Tr. p. 208]. Bankruptcy was contemplated and advice given to the bankrupt by Mr. Granger long prior to the transactions which were the subject of the action which gave rise to this appeal. [See Tr. pp. 299; Tr. p. 293; Tr. of Record p. 277; Tr. of Record p. 267], and at the time of the formation of Pacific Palmdale Development Company hereinafter discussed, the bankrupt and Mr. Granger were discussing the filing of bankruptcy proceedings. [Tr. of Record, p. 256].

In March of 1954 Philip Bloom, the bankrupt's wife and Merrill L. Granger, attorney for the bankrupt, signed Articles of Incorporation of the corporation ultimately incorporated on April 6, 1954, and the Articles of Incorporation were not forwarded to the Secretary of State of the State of California until on or about April 3, 1954.

At the time of the signing of the Articles of Incorporation the signatures thereto were not properly notarized and the notary was not present during the signing of the Articles by Philip Bloom [Tr. of Record, p. 301]. Mr. Bloom was informed that the Articles of Incorporation would be filed immediately after the signing of the Articles of Incorporation, notified the other incorporators that he wished to withdraw and that he would assert no interest in and to the Pacific Palmdale Development Company [Tr. of Record, p. 357; Tr. of Record, p. 283; Tr. of Record, p. 284; Tr. of Record, p. 289]. Mr. Bloom at

no time had any interest in any grain bin transaction, [Tr. of Record, p. 290], and the only transaction he had any interest in was completely abortive [Tr. of Record, p. 306].

Pacific Palmdale Development Company did not issue any stock [Tr. of Record, p. 221] and had no capital [Tr. of Record, pp. 324 and 330]; did not keep any ledgers or accounts, and had no capital structure or financial transactions beyond its mere incorporation. [Tr. of Record p. 324]. Allegedly, the bankrupt's attorney was to have a 12 per cent interest in the corporation; the wife of the bankrupt a 44 per cent interest, and the son of the bankrupt, William Hudson, a 44 per cent interest.

The wife of the bankrupt was a housewife, with five children, who had never been in business for herself and had no training in any commercial proceedings. [Tr. of Record, p. 203]; she held nothing other than property which was the result of the earnings of the bankrupt, and contributed nothing to the corporation other than nominal incorporation costs. [Tr. of Record, p. 204].

At the time of incorporation the son of the bankrupt, William Hudson, resided at Portland, Oregon with his family; was twenty-seven years of age; was to contribute nothing to the corporation other than his labor as a superintendent in the fabrication of the bins, and was paid a salary for his services as such superintendent. [Tr. of Record, pp. 220 and 221].

On or about April 2 or April 3, 1954 the bankrupt contacted Lloyd R. Reeve, informing him that he wanted to find someone to go in with him on a grain bin deal, making no mention of a corporation. It was proposed that Mr. Reeve finance the submission of bids to the

Commodity Credit Corporation and the manufacturing and erection of bins. [Tr. of Record, pp. 72 to 74].

On April 3 or April 4, 1954 a firm understanding was reached between the bankrupt individually and Lloyd R. Reeve that Mr. Reeve would finance the project and that after expenses of the deal were determined each was to take half of the profits, and it was only on April 5 or April 6, 1954 that any discussion was had regarding the Pacific Palmdale Development Company. [Tr. of Record, p. 76], and the bankrupt represented at that time that he was the Pacific Palmdale Development Company [Tr. of Record, p. 77].

On numerous occasions the bankrupt represented to Mr. Reeve and to Mr. Carl Minton, Sr., the attorney for Mr. Reeve, that he was the sole owner of the Pacific Palmdale Development Co. [Tr. of Record, p. 81; Tr. of Record, p. 153]; represented that he had organized Pacific Palmdale Development Co. to benefit himself [Tr. of Record, p. 82], and Mr. Merrill L. Granger, the attorney for the bankrupt, represented that Mr. Hudson had a corporation [Tr. of Record, p. 161].

At this point it is worthwhile to note that the Petition in Bankruptcy was filed on April 19, 1954 by a voluntary Petition in Bankruptcy and the chronology of events relating to a contract between the bankrupt or his alter ego, Pacific Palmdale Development Company, and Lloyd R. Reeve, Inc.

On or about April 2nd or April 3rd, 1954, some 16 or 17 days prior to bankruptcy, negotiations commenced between Mr. Reeve and the bankrupt relating to a joint venture for the erection of train bins for Commodity Credit Corporation [Tr. pp. 71 to 76.]

On April 3, 1954 the Articles of Incorporation were mailed to the Secretary of State of the State of California, *supra*. On April 7, 1954 Mr. Reeve and Mr. Hudson met in Washington, D. C. for the purpose of submitting bids. [Tr. pp. 78 and 79]. On April 7, 1954 Hudson, ostensibly on behalf of Pacific Palmdale Development Company, executed a joint venture contract with Reeve through Reeve's corporation, Lloyd R. Reeve, Inc. [Tr. pp. 78, 79. Exhibits designated in Designation of Record on Appeal].

On April 6, 1954 the Pacific Palmdale Development Company was incorporated. (See answer of bankrupt and Pacific Palmdale Development Company; exhibits designated in Designation of Record on Appeal).

On April 8, 1954 Pacific Palmdale Development Company, through its directors, allegedly passed a resolution whereby the bankrupt was authorized to act as treasurer of Pacific Palmdale Development Company for the sole and limited purpose of executing the contract between Lloyd R. Reeve, Inc. and Pacific Palmdale Development Company. (See Exhibits designated in the Designation of Record on Appeal).

On April 9, 1954, ten days prior to bankruptcy, the bid was submitted to Commodity Credit Corporation [Tr. p. 92] and on April 17, 1954, two days prior to bankruptcy, a conditional acceptance was forwarded to Lloyd R. Reeve, Inc. by the Commodity Credit Corporation [Tr. p. 93], and on April 19, 1954, conveniently the day of bankruptcy, Lloyd R. Reeve, Inc. accepted the bid of Commodity Credit Corporation. [Tr. pp. 93, 94]. (Answer of respondents designated as an exhibit in the Designation of Record on Appeal.)

On May 21, 1954, without an assignment having been made by Pacific Palmdale Development Company, $1,000.00 was paid by Lloyd R. Reeve to the bankrupt as part of the profits of the aforementioned contract with Commodity Credit Corporation. This is admitted by the bankrupt and the Pacific Palmdale Development Company. [Tr. p. 86].

On May 21, 1954, by and with the assignment of Pacific Palmdale Development Company, the bankrupt was paid an additional $15,000.00 on account of profits and this was was also admitted by the answer of the bankrupt and the Pacific Palmdale Development Company [Tr. p. 96] and on December 17, 1954 the bankrupt was paid an additional $5,000.00 by and with the assignment of the Pacific Palmdale Development Company on account of profits due under the contract. This is admitted by the answer of the bankrupt and the Pacific Palmdale Development Company. There remains on hand approximately $23,000.00 from the profits of the joint venture which are payable to either the Pacific Palmdale Development Company or this bankruptcy estate. (See Answer of defendant among Exhibits).

On April 20, 1954, one day subsequent to bankruptcy, the Board of Directors of Pacific Palmdale Development Company passed a resolution which, among other things, contained a resolution that the first $50,000.00 payable to Pacific Palmdale Development Company under the joint venture contract of Lloyd R. Reeve, Inc. be payable to the bankrupt. (See Exhibits on file and designated in the Designation of Record on Appeal).

During all the times mentioned the bankrupt and his attorney, Merrill L. Granger, had an agreement whereby

the bankrupt was to pay his attorney 12 per cent of his earnings as attorney fees for services rendered. [Tr. p. 326]. Likewise, Mr. Granger was granted a 12 per cent interest in the Pacific Palmdale Development Company [Tr. p. 327]. Out of the funds received by Hudson, the bankrupt, Merrill L. Granger received 12 per cent of $20,000.00 received by the bankrupt. [Tr. p. 327].

On April 19, 1954 the within bankruptcy proceedings were commenced by the filing of voluntary Petition in Bankruptcy, and the matter proceeded as a no-asset estate. No interest of the bankrupt in and to the Pacific Palmdale Development Company or any profits arising by virtue of the joint venture agreement heretofore referred to was made in the Schedules of the bankrupt. The bankrupt listed creditors in a total amount of approximately $350,000.00 and the Trustee now has on hand a nominal sum of approximately $150.00.

More than a year prior to the institution of the proceedings the above transactions came to the attention of the Trustee from a third party, and it was then and only then that the proceedings giving rise to this appeal were instituted.

Issues Involved.

The appellee is of the opinion that the only issues involved are as follows:

(a) Whether or not the Pacific Palmdale Development Company was the alter ego of the bankrupt;

(b) Whether or not the assets earned under the joint venture contract between the Pacific Palmdale Development Company and Lloyd R. Reeve, Inc. are assets of this bankrupt estate.

ARGUMENT.

I.

The Pacific Palmdale Development Company Was Organized Solely for the Purpose of Defrauding Creditors of the Bankrupt.

The evidence presented at the trial before the Referee was direct and conflicting regarding the purpose of the incorporation of Pacific Palmdale Development Company. The bankrupt and his attorney testified that Mr. Granger, the attorney for the bankrupt, conceived the idea of incorporation and that this was merely a method whereby Mr. Granger would utilize the services of the bankrupt. At the conclusion of the hearing the Referee stated:

> "The Court has made allowances for any possible bias or prejudice on the part of Mr. Reeve and Mr. Minton. In fact, it appears to the Court that if you entirely ignore the testimony which has been given by Mr. Reeve and Mr. Minton alone, that the conclusion is inescapable beyond a shadow of doubt that the Pacific Palmdale Development Company, and the preparation of the Articles of Incorporation in connection therewith, was originally intended to be used by Mr. Hudson in a real estate development transaction with Mr. Bloom, but that Mr. Bloom withdrew from that corporate setup, and that this hollow shell of a corporation, known as Pacific Palmdale Development Company, was used merely as a conduit or as an instrumentality to further the interests of Mr. Hudson, and to a lesser extent, the portion of the earnings which Mr. Granger, as his attorney, would receive for his legal services in that connection." [Tr. of Record, p. 358].

The following facts testified to by the bankrupt and the bankrupt's attorney, and the other witnesses, conclusively

demonstrate that the Pacific Palmdale Development Company had no purpose save and except as an instrumentality to remove assets of bankrupt from the reach of creditors:

> The bankrupt's assignment for benefit of creditors and the knowledge of the bankrupt and his attorney that the same was without release, [Tr. pp. 232, 233, 316 to 319]; the preparation and execution of an agreement allowing the wife to retain her earnings as separate property, the purpose being to enable the bankrupt to get started in business again without creditors of the bankrupt being able to attack his earnings [Tr. pp. 232, 233 and Exhibit "A" of the proceedings before the Referee]; the familiarity of the attorney for the bankrupt with creditors' rights law and his former specialization in that field [Tr. of Record, pp. 315 to 316]; the lack of any special knowledge or skill regarding construction of grain bins or the submission of bids on the part of the bankrupt's attorney [Tr. p. 326]; the personal knowledge and skill of the bankrupt regarding submission of bids and the erection and construction of grain bins [Tr. p. 272, 274]; the fact that the bankrupt was advised on many occasions that he could not accumulate substantial earnings without a release from his creditors [Tr. of Record, pp. 267 and 197]; the fact that Articles of Incorporation were signed more than a month prior to their filing and during the interim the entire purpose of the corporation had changed, and one of the incorporators gave notice of his withdrawal as an incorporator prior to the filing of the Articles of Incorporation, [Tr. of Record, pp. 357, 283, 284, 289 and 290]; the fact that the original purpose

of the corporation was not accomplished and was abortive [Tr. of Record, p. 306]; the fact that negotiations commenced between the bankrupt and Lloyd R. Reeve on April 2nd or 3rd, 1954 [Tr. of Record, pp. 72 to 74], and on or about that date the purpose of the corporation was changed and the Articles of Incorporation forwarded to the Secretary of State for filing; the fact that the bankrupt conducted all negotiations with Lloyd R. Reeve and arrived at a firm understanding prior to any written agreement or any mention of the Pacific Palmdale Development Company [Tr. of Record pp. 72-76]; the fact that the bankrupt on numerous occasions represented that he owned Pacific Palmdale Development Company or was personally the Pacific Palmdale Development Company [Tr. of Record, pp. 77, 81, 153]; in fact, the bankrupt represented that he organized Pacific Palmdale Development Company himself; the fact that the attorney for the bankrupt represented to the attorney for Lloyd R. Reeve that Mr. Hudson had a corporation; the fact that at the time of the drafting of the Articles of Incorporation and at the time of the filing of Articles of Incorporation with the Secretary of State, Merrill L. Granger, the attorney for the bankrupt, was advising the bankrupt regarding bankruptcy [Tr. of Record, p. 256]; the fact that the joint venture contract between Lloyd R. Reeve, Inc., and Pacific Palmdale Development Company contained terms to the effect that the personal services of the bankrupt be furnished and that the Pacific Palmdale Development Company could assign their interest to the bankrupt, (See Agreement of April 7, 1954 among Exhibits designated);

the fact that the bankrupt personally went to Washington, D. C. and assisted in the preparation of the bids submitted to the Commodity Credit Corporation and was the only person among those involved who had any special knowledge or skill regarding the preparation of such bids for erection of grain bins; the fact that no stock was ever issued by Pacific Palmdale Development Company and no application for a Permit to Issue Stock was ever made to the Corporation Commissioner of the State of California [Tr. of Record, p. 221]; the fact that Pacific Palmdale Development Company had no capital [Tr. of Record, pp. 324 and 330]; did not keep any ledgers or accounts and had no capital structure or financial transactions beyond its incorporation [Tr. of Record, p. 324]; the fact that the incorporators consisted of the bankrupt's attorney, who was allegedly to have a 12 per cent interest, which, coincidentally, was identical with an attorney fee arrangement between the bankrupt and the bankrupt's attorney which existed prior to bankruptcy [Tr. of Record, pp. 326-327], the son of the bankrupt, who resided in Portland, Oregon and was a mere 27 years of age and contributed nothing to the corporation [Tr. of Record, pp. 20 and 21], and the wife of the bankrupt, a housewife with five children, with no training in commercial pursuits and who owned no property other than property which was the result of earnings of the bankrupt [Tr. of Record, pp. 203 and 204]; the fact that on April 8, 1954 the directors of the Pacific Palmdale Development Company passed a resolution whereby the bankrupt was authorized to execute the agreement; the fact that the acceptance

of the Commodity Credit Corporation was not accepted by Lloyd R. Reeve, Inc. until April 19, 1954, the day of bankruptcy; the fact that on April 20, 1954, one day subsequent to bankruptcy, the Board of Directors of Pacific Palmdale Development Company passed a resolution whereby the first $50,000.00 of the profits of Pacific Palmdale Development Company were assigned to the bankrupt (Answer of the bankrupt, among exhibits designated); the fact that approximately thirty-one days after bankruptcy the bankrupt was paid $15,000.00 [Tr. p. 96] and was paid an additional $6,000.00 constituting all funds paid over to Pacific Palmdale Development Company by Lloyd R. Reeve, Inc.

From the above evidence it should at once be apparent that the bankrupt could have contracted directly with Lloyd R. Reeve, Inc. without the medium of a corporation, and that all funds received as the Hudson or Pacific Palmdale Development Company share, were paid directly to Hudson. It should also be apparent that the only services rendered were services rendered by Hudson, that and that no services whatever were rendered by the Pacific Palmdale Development Company. In view of the knowledge of insolvency of the bankrupt and his attorney and the chronology of events above set forth, it is difficult, if not impossible, to believe the testimony of the bankrupt and of the bankrupt's attorney that the Pacific Palmdale Development Company was a legitimate corporation wholly dominated and controlled by parties independent of the bankrupt and organized only for the purpose of benefiting the bankrupt's attorney, and on the contrary it is at once apparent that the only purpose this corporation served was to insulate the bankrupt from his creditors.

This is further buttressed by the scathing denunciation delivered by the trial judge, the Referee in Bankruptcy, which may be found at pages 358 and 359 of the Transcript of Record, and the Findings of Fact and conclusions of Law of the Referee, specifically finding of intent to hinder, delay and cheat the creditors of the bankrupt, said Findings having been reviewed and affirmed by United States District Court. [See Findings of Fact XLVII, Tr. p. 32, Conclusion of Law X, Tr. p. 36].

II.

The Pacific Palmdale Development Company and John Lucas Hudson Should Not Be Heard to Complain of Lack of Proof of Divisibility of the Fund Created Contrary to Their Position Taken During the Trial.

During the trial of this matter the attorney for Pacific Palmdale Development Company and John Lucas Hudson consistently took the view that any proof as to the divisibility of the contract between Lloyd R. Reeve and Pacific Palmdale Development Company of April 7, 1954 so as to divide services rendered prior to bankruptcy from those rendered subsequent to bankruptcy was immaterial and made numerous objections which were sustained by the trial Court regarding the materiality of this evidence. [See question asked on page 84 of the Tr. of Record and the Objections of Mr. Granger on that page]. At page 87 of the Tr. of Record the following question was asked:

> "Q. (By Mr. Bartley): Mr. Reeve, you have just heard the Court read that portion of this contract which is Trustee's Exhibit No. 1, which relates to the services of John L. Hudson in procuring and performing contracts from the Commodity Credit Corporation.

> Now, to the best of your knowledge and as best as you can draw any cleavage and distinction between procurement of the contract and performance of the contract, what percentage of the servcies of Mr. Hudson was to be for the procurement of contracts and what percentage was to be rendered to your corporation in the performance of the contract."

And on page 88 the objection of Mr. Granger to the above question was:

> "Mr. Granger: *That is objected to as incompetent, irrelevant and immaterial . . .*"

[See questions and objections as to divisibility on page 123 and 124 of the Transcript of Record]. [See questions and objections on page 132 of Tr. of Record].

The above references show that at the trial of the matter the introduction of evidence regarding the divisibility of the consideration to be paid to Pacific Palmdale Development Company and the introduction of evidence rgarding the major inducment to Lloyd R. Reeve for entering into the joint venture contract were prevented by objections from counsel for the appellants regarding materiality of such evidence. The appellant should not now be permitted to take advantage of his own act of preventing testimony from being introduced by reversing his position and now arguing that such evidence was vital to the trustee's case, was material and that there was a lack of any proof regarding the same, when his whole position at the trial was that the same was irrelevant and immaterial.

III.

The Major Inducement of the Joint Venture Contract Was Hudson's Ability for Procuring Acceptance of Bids.

The evidence at the trial and the inferences therefrom make it quite clear that there never would have been a joint venture contract but for the fact that Hudson had experience in submitting plans and specifications, had an invitation to bid and have bids accepted by the Commodity Credit Corporation, [See Tr. of Record, p. 72]; that Hudson contacted Reeve and advised him that he had an invitation to bid and wanted to find someone who would go in with him on a grain bin deal, and the Transcript of Record where Hudson represented that he was going to put experience into the deal if Reeve would finance it. [Tr. of Record, pp. 73 and 74]. In answer to the question "By the grain bin work and the leg work, do you mean the procurement of contracts?" "A. And the manufacturing and erection of the bins. He was to assist me in all that work, yes."

It is uncontrovertible that Hudson went to Washington, D. C. and assisted in the preparation and presentation of the bids to the Commodity Credit Corporation. [See Tr. of Record, pp. 91, 136, 137 and 223]. Prior to the trip to Washington and the signing of the written contract of the joint venture Reeve and Hudson went over plans, made estimates, took off material lists, made arrangements for an influence man, etc. [Tr. of Record, pp. 136, 137]. Thus it is apparent that estimates and plans

were all prepared by the bankrupt and his assistants or associates prior to the time that Reeve and Hudson left Washington on April 9, 1954, some ten days prior to bankruptcy, and prior to bankruptcy the profits had been estimated and there merely remained the acceptance of the bid by Commodity Credit Corporation, which took place on the 17th day of April, 1954, *supra,* and the acceptance by Reeve which took place on the day of bankruptcy, April 19, 1954, *supra.* When the plans and specifications, lists of materials and estimates were made all preliminary work had been concluded and the work was performed by subcontractors to erect the grain bins in the field.

It is the contention of the appellee that once the plans and specifications had been drawn and accepted, the lists of materials and estimates made, that the nature of the services of Hudson in the performance of erection of the grain bins was not of such a special nature that any engineer or contractor could not have read the plans and specifications and arranged the fabrication of the grain bins, and that the contract was therefore assignable as to the performance features. Certainly, the major inducement to Reeve was Hudson's ability to prepare a bid from prior plans and specifications and to have the same accepted by the Commodity Credit Corporation.

IV.

At the Date of Bankruptcy the Bankrupt or the Pacific Palmdale Development Company Had a Vested Interest in and to the Proceeds Arising From the Acceptance of the Bids From the Commodity Credit Corporation.

A reading of the contract as a whole between Lloyd R. Reeve and the Pacific Palmdale Development Company reveals that after certain sums were paid to other parties, the net profits were to be divided equally between Lloyd R. Reeve and the bankrupt. The reference to net profits relates to profits arising by virtue of contracts for the erection of grain bins with the Commodity Credit Corporation. At the time of bankruptcy these bids had been submitted and accepted by the Commodity Credit Corporation. As pointed out in the argument, paragraph No. III above, prior to bankruptcy Hudson had performed the work which was the major inducement for Reeve entering into a contract with the Pacific Palmdale Company. Estimates had been made and a large profit was anticipated. Hudson could have assigned his interest to another party prior to bankruptcy.

Much is made by the appellants of the fact that it was some days after bankruptcy that the bankrupt agreed to accept the first $50,000.00 of the net profits of the transaction and the bankrupt testified at some length that he merely expected to receive something for his services, and that no agreement had been made prior to his departure for Washington, or prior to his bankruptcy as to what compensation he would receive from the Pacific Palmdale Development Company.

We respectfully submit that this testimony was simply unbelievable in view of the facts set forth in the appellee's

Statement of the Case, *supra,* and the argument set forth in paragraph I of the Argument, *supra,* to the effect that Pacific Palmdale Development Company was organized solely to hinder, delay, cheat or defraud creditors of the bankrupt. It is simply unbelievable that Hudson personally contacted Reeve, offered to arrange the submission of the bids, provided the plans and specifications and his technical knowledge in return for financing by Reeve, all without any definite understanding as to what his share of the profits would be. The whole purpose of the Pacific Palmdale Development Company was to prevent creditors of Hudson from being able to attach or reach his interest in this very grain bin deal which so conveniently took place at or about the identical time of Hudson's bankruptcy. The law of the State of California is clear regarding assignments. *Cox v. Hughes,* 10 Cal. App. 553 (1909) at 561 holds that equity will support not only assignments and choses in action and all contingent interests and exceptions, but also things which have no present actual or potential existence but rest in mere expectancy.

This was not the situation of a contemplated contract between the parties, but a situation where an actual contract had been executed prior to bankruptcy, calling for personal services of the bankrupt, a substantial portion of which had been performed prior to bankruptcy; a situation where fabulous profits were anticipated by the parties to the contract from a third contract, the third contract being the contract for the Commodity Credit Corporation. The contract with the Commodity Credit Corporation was not a mere expectancy at the time of bankruptcy, but bids had been submitted and accepted by both parties at least on the very day of bankruptcy.

This was not a situation were future earnings from personal services was anticipated, but was a profit-sharing venture wherein profits had been estimated and were clearly anticipated prior to bankruptcy. This situation is not analogous to a situation where a bankrupt or wage earner or professional man is anticipating that he might be employed sometime in the future. This is not a situation where wages are involved, and if we disregard the entity of the Pacific Palmdale Development Company, was a situation where a joint venture agreement was entered into between two parties to share profits.

It is therefore respectfully submitted that the actual effect of the entity known as the Pacific Palmdale Development Company was to insulate the bankrupt from the claims and demands of his creditors as regards any profits or expected profits he had from the contracts relating to the erection of the grain bins.

V.

The Pacific Palmdale Development Company Was and Is the Alter Ego of the Bankrupt.

The arguments heretofore set forth demonstrate that the only purpose of the Pacific Palmdale Development Company was to hinder, delay, cheat or defraud creditors of the bankrupt, and that they actually did hinder, delay and cheat creditors of the bankrupt. The arguments heretofore advanced also demonstrate that the Pacific Palmdale Development Company had no capital structure, kept no ledgers, did not issue stock, and had only nominal shareholders consisting of the bankrupt's wife, son and

attorney, each of which contributed nothing to the corporation, and that but for concern about his creditors the bankrupt could have contacted directly with Lloyd R. Reeve, Inc. It has also been demonstrated that the bankrupt received all of the profits which were allegedly payable to the Pacific Palmdale Development Company. These arguments are incorporated herein and made a part hereof as fully as if set forth in detail herein.

> "While a corporation is usually regarded as an entity separate and distinct from its stockholders, both law and equity will, whenever necessary, circumvent fraud or protect the rights of third parties, disregarding this distinct existence and treat them as identical."

Katenkamp v. Superior Court, 16 Cal. 2d 629, 700, 108 P. 2d 1:

> "It is not necesary that actual fraud be shown. It is sufficient if a refusal to recognize the fact of the identity of the corporate existence with that of the individual would bring about inequitable results."

Wenban Estate Inc. v. Hewlett, 193 Cal. 675, p. 698, 227 Pac. 723.

Minifie v. Rowley, 187 Cal. 481, 202 Pac. 673.

Jackson v. American Bearing, 89 Cal. App. 2d 256.

Marr v. Postal Union Life Insurance Company, 40 Cal. App. 2d 673, 105 P. 2d 649.

See:

12 Cal. Jur. 2d p. 604, Article 8 and cases cited.

VI.

The Incorporation of the Pacific Palmdale Development Company and the Agreement Between the Pacific Palmdale Development Company and the Bankrupt Were Void as a Fraud on the Creditors of the Bankrupt.

If we were to accept the testimony of the bankrupt to the effect that he had no agreement personally regarding the amount he was to receive for his services rendered to Lloyd R. Reeve or the Pacific Palmdale Development Company as true, the entire transaction would be voidable under Section 70-a-4 of the Bankruptcy Act, U. S. Code, Title 3, Chapter 7 (Sec. 110), and the Bankruptcy Act, Section 70-a-5 for the reason that the bankrupt must have agreed to perform services in connection with the joint venture contract for Lloyd R. Reeve, Inc. as shown by the very contract executed between the Pacific Palmdale Development Company and Lloyd R. Reeve, Inc. which promised to make available the services of the bankrupt. As the bankrupt promised to render services, any transfer of his expected earnings from the performance of such services without consideration would, under Section 70, be a fraud on creditors. The record illustrates that such a transfer was made in that Pacific Palmdale Development Company was incorporated and the son and wife of the bankrupt were to be the principal shareholders and thereby to receive the profits arising by virtue of the joint venture contract, and they and each of them contributed nothing whatever to the corporation or to the bankrupt in return for his promise to perform services. The promise to perform services was therefore without adequate or full consideration or any consideration whatever.

The fact that the bankrupt had been receiving advice regarding his creditors, *supra,* had been contemplating bankruptcy, *supra,* had made a prior assignment for benefit of creditors, and had not been released, *supra,* clearly demonstrate that the bankrupt was insolvent at the time of the various transactions herein mentioned.

> "A voluntary conveyance made by a debtor to a member of his family while insolvent, was in contemplation of insolvency, is conclusively presumed to be speculative as to existing creditors."
>
> *Adams v. Prather,* 176 Cal. 33, 167 Pac. 534;
>
> *Carter v. Carter,* 55 Cal. App. 2d 13, 130 Pac. 2d 186.

VII.

The Right to Receive Money Due or to Become Due Under a Contract May Be Assigned.

In general, see 5 Cal. Jur. 2d p. 286, Sec. 13, and *Smitton v. McCullough,* 186 Cal. 530, 189 Pac. 686.

Though the contract itself is, by its terms, declared to be non-assignable or non-assignable because it involves personal skill and confidence.

> *Green v. Mullaly,* 211 Cal. 77, 293 Pac. 619.

The fact that the assigned claim is for money to become due under a contract conditioned upon the future performance of undertakings by the assignor does not destroy its assignability under the argument that the debt has no present existence or is merely a possibility provided a satisfactory basis exists of finding that the future debt has a potential present existence.

> *Lynit v. Alturas School District,* 24 Cal. App. 426, 5 Cal. Jur. 2d 283.

The assignment of claims for wages to be earned in the future affords a common illustration of the application of rule.

5 Cal. Jur. 2d 288, 5 Cal. Jur. 2d 295, Sec. 23;

Cox v. Hughes, 10 Cal. App. 553;

Walter v. Rich, 179 Cal. App. 139;

Silverstein v. Oakland Title Insurance and Guarantee Company, 122 Cal. App. 73.

VIII.

The Findings of the Referee Should Not Be Reversed Unless Clearly Erroneous.

See:

Gold v. Gerson, 225 Fed. 2d 859, C. C. A. Ninth (1955).

These writers will not attempt to point out to the learned Court the law on whether or not they are bound by the trial Court's Findings of Fact. However, the appellants attempt to point out to the Court in the first paragraph of the appellant's argument that the Court is not bound by the trial Court's Findings of Fact, and cited numerous instances upon which they state that there is no conflict in evidence. We differ materially from the version of the appellants and believe that the record as a whole will demonstrate that every material issue was controverted by the appellants at the trial and that there was a direct conflict of evidence as regards each material point of the case.

There was a definite conflict in evidence as to whether Mr. Philip Bloom had any interest in the Pacific Palmdale Development Company or in the grain bin deal as evidenced by Bloom's testimony that he resigned on April

12, 1954 and disavowed any interest in the grain bin deal, *supra;* the written resignation of Mr. Bloom which was offered in evidence, *supra,* and the testimony of Mr. Minton that Bloom indicated to him that he had signified his resignation from Pacific Palmdale Development Company several weeks in advance of its incorporation, *supra.* It was also evidenced that the entire Pacific Palmdale Development plan was abortive, *supra.*

There was a definite conflict in evidence regarding whether or not Mr. Bloom was interested in getting into the grain bin deal in early April, as evidenced by the testimony of Mr. Bloom and the testimony of Mr. Minton that Bloom had withdrawn from the corporation several weeks prior to the grain bin deal, *supra.*

There was a definite conflict in evidence regarding Mr. Granger's advice regarding the financial affairs of the bankrupt as evidenced by both the testimony of the bankrupt's attorney and the bankrupt cited, *supra,* and the fact that the attorney for the bankrupt was preparing a Petition in Bankruptcy and advising the bankrupt in regard to bankruptcy at the time of the entire transaction, and had at a prior date prepared an agreement whereby the earnings of the wife were her own sole property, *supra;* the limiting of the authority to Hudson as an officer of the corporation at the time of the signing of the joint venture agreement, *supra.*

Item 2 in paragraph I of the appellants' argument is the very matter upon which there was more conflicting evidence than any other item, among which were various statements of Hudson to Minton and to Reeve that he owned the Pacific Palmdale Development Company and that he organized the same to benefit himself as well as the fact that Hudson conducted all negotiations with

Reeve, all sums realized were paid to Hudson, Granger had a nominal interest of 12 per cent which co-incidentally was identical with his prior attorney fee arrangment with Hudson, and many other facts testified to which made it clear that this version of the hearing testified to by Mr. Granger simply was not true. [See various references in the Transcript, *supra*].

As to Item 13 of paragraph I of the appellants' argument, there again was a substantial conflict of evidence, *supra*.

As to Item 15 of paragraph I of the appellants' argument, the bankrupt himself admitted on the stand that he expected to be paid for his services before he went to Washington, D. C., and the fact that he conducted all negotiations, all of the stockholders were either his relatives or his attorney, the corporation had no capital structure, and no purpose save and except to insulate Hudson from his creditors, plus the fact that conveniently the very employment agreement referred to in this argument was made one day after bankruptcy, all raise logical inferences that there was in fact no employment agreement and that the contract between Reeve and the Pacific Palmdale Development Company was in fact a joint venture agreement strictly between Hudson and Lloyd R. Reeve and that even if there were an employment agreement the same existed prior to bankruptcy.

The cases cited by the appellants on page 9 of the appellants' brief and on page 11 of the appellants' brief merely illustrate the well known rule of law that an

Appellate Court will not accept the findings of the trial Court if a plain mistake is shown. They do not stand for the proposition that there should be a trial *de novo* in the Appellate Court, nor do they stand for the proposition in cases such as the instant case where there is conflicting evidence on all material issues that the Appellate Court should not be bound by the trial Court's findings.

It is therefore respectfully submitted that the law in *Gold v. Gerson, supra,* is applicable to the instant case rather than the various cases cited by the appellants.

IX.

The Entire Argument of the Appellants Is Based on the View That Hudson Merely Had an Agreement to Perform Personal Services Which Was in the Nature of an Employment Contract.

An examination of the argument of the appellants contained in paragraphs II, III, VI, VII and VIII reveals that again and again counsel for the appellants takes the position that everything payable to the bankrupt was in the nature of wages. It is argued that these are wages and wages are non-assignable, etc.

We believe that an examination of the various facts testified to and the very findings of the Referee. See Findings XXV, p. 25 Tr.; Findings of Fact XLVII, p. 32 of Transcript, and Conclusion of Law No. II, p. 34 of Transcript, and the appellee's Statement of the Case and references to the transcript contained therein, *supra;* where the evidence and the findings clearly demonstrate that the Pacific Palmdale Development Company was con-

ceived and incorporated for the purpose of hinder, delaying, cheating and defrauding creditors of bankrupt; where it is shown that the bankrupt had personally made an agreement with Lloyd R. Reeve prior to any mention of the Pacific Palmdale Development Company; where it is shown that the bankrupt could have executed a written agreement directly with Lloyd R. Reeve, Inc.; where it is shown that the agreement between Lloyd R. Reeve and the Pacific Palmdale Development Company was actually an agreement directly between the bankrupt and Lloyd R. Reeve, Inc.; where it is shown that the bankrupt himself received all of the profits allegedly due Pacific Palmdale Development Company, and where the chronology of events clearly demonstrates that the only purpose served by the Pacific Palmdale Development Company was to hinder, delay, cheat and defraud creditors of the bankrupt.

An examination of the joint venture agreement between Reeve and the Pacific Palmdale Development Company [Trustee's Ex. I at trial, designated among Exs. designated] reveals that this is purely and simply an agreement to divide the net profits of any grain bin contracts awarded to and performed by the parties during the year 1954. It is not an employment contract, nor does it purport to employ the bankrupt. The bankrupt or Pacific Palmdale Development Company is a principal in the contract and, while required to furnish services, the bankrupt is not an employee of Lloyd R. Reeve, Inc. We submit that the true nature of the contract is a joint venture contract to share in the profits of the grain bin transactions and that is exactly what took place shortly after bankrupt, and that all arguments regarding the performance of employment are therefore inappropriate.

X.

There Was a Contract in Existence Between the Commodity Credit Corporation and the Bankrupt at Time of Bankruptcy.

The evidence shows the Commodity Credit Corporation accepted the bids from Reeve on April 17, 1954, and that Reeve in turn accepted acceptances of the Commodity Credit Corporation on the day of bankruptcy. Not one scintilla of proof by way of defense was offered by the bankrupt or the Pacific Palmdale Development Company as to the precise terms of the contract between the Commodity Credit Corporation and Lloyd R. Reeve, Inc. The contract was admitted in the answer of the defendants. The fact that the profits were received under a contract was likewise admitted. No proof was offered regarding the bond requirements of the Commodity Credit Corporation. It is therefore submitted that there is no proof that the contract between the Commodity Credit Corporation and Lloyd R. Reeve was conditioned upon the posting of a bond.

The citations in the appellants' Argument No. 2 which are found on page 12 of the appellants' Argument, which refer to the Restatement of the Law of Contracts and to Williston on Contracts refer to counter offers and conditional acceptances by offerees, and throw no light whatever upon the problem at hand, nor do they reinforce the propositions asserted by the appellants.

The case of *Flynn v. Dougherty,* 3 Cal. Unrep. 412, 26 Pac. 831, refers to a contract to furnish stone in connection with a building to be erected for the State of California. It holds that the furnishing of a bond was a

condition precedent to the right of the materialman to file an action for damages and is a ruling on a motion for dismissal or a nonsuit. It does not stand for the proposition for which the appellant cited it.

XI.

That It Would Be Inequitable to Not Penetrate the Veil of the Pacific Palmdale Development Company Has Been Amply Demonstrated.

See Appellee's Argument No. V regarding the proposition that the Pacific Palmdale Development Company was the alter ego of the bankrupt. See appellee's Argument No. I that the only purpose of the Pacific Palmdale Development Company was fraud. See appellee's Argument No. IV that at the date of bankruptcy the bankrupt had a vested interest in the proceeds.

Cases cited in paragraph IV of the appellants' argument merely illustrate the position that the Court can pierce the corporate veil and refuse to recognize the separate entities, if to recognize the same would sanction a fraud or promote injustice.

We agree with the appellants' brief that the Bankruptcy Act is a benevolent statute and that it contemplates that an honest debtor may, under its influence, rehabilitate himself and submit that this was not an honest debtor and that the Referee had before him considerable evidence regarding the fraudulent intent of the bankrupt and his attorney and made detailed Findings of Fact regarding the fraudulent intent of both the bankrupt and the bankrupt's attorney, and that these Findings are adequately supported by the record.

XII.

Whether or Not a Wife Must Consent to an Assignment of Future Wages Is Immaterial.

The appellants overlooked the fact that the interest of Hudson was not wages but was an interest in profits arising under a joint venture contract. There is no question before the Court as to whether or not the bankrupt could have assigned wages. We are dealing with a present vested interest of the bankrupt in and to a share of profits, and we submit that the entire argument contained in paragraph No. 4 of the appellants' argument is irrelevant insofar as it relates to an assignment or assignability of wages.

XIII.

In a Situation Involving Actual Fraud the Court Should Place the Burden Upon the Instigator of the Fraud, to Prove Separability of Consideration.

The case of *Miller v. Wooley,* 141 F. 2d 837, cited by the appellants on page 21 of the appellants' brief has no application whatever to the instant case as this was a Chapter XI proceeding involving the Estate of John Barrymore and the issue involved was whether or not an attorney could retain a divorce fee paid him by Barrymore during the pendency of the Chapter XI proceedings. This case was in no way analogous to the instant case, nor was any rule of law therein announced in any way related to a situation such as we have in the instant case or the questions involved such as are involved in the instant proceedings.

The case of *in re Leibowitt,* 93 F. 2d 333, C. C. A. Third (1937), 115 A. L. R. 623, cited by the appellants on page 21 of the appellants' brief may be distinguished from the case at bar in that the bankrupt listed the com-

missions in his schedules and in that there was no fraud whatever involved. The only issue before the Court was whether or not the commissioners should be divided into those earned prior to bankruptcy and those earned subsequent to bankruptcy.

In re Seiffert, 18 F. 2d 444, D. C. D. Montana (1926) cited by the appellants on page 21 of the appellants' brief, related to a share crop agreement and may be distinguished from the instant case in that that case related solely to objections to the discharge of the bankrupt and in a discharge situation the degree of proof required by the Referee is considerably higher than the degree of proof required in the instant case. That case also involved an option to purchase. This case likewise did not involve any deliberate fraud or fraudulent scheme on the part of the bankrupt.

In re Thomas, 204 F. 2d 788, C. C. A. Seventh (1953) cited on page 22 of the appellants' argument may be distinguished in that the same involved a Petition to re-open instituted some eleven years after adjudication and rested on the fact that there was no finding regarding the portion of the fee earned prior to bankruptcy and was decided on the basis that the amount involved arose by virtue of trustee's fees allowed by a State court which did not occur until the bankrupt made a final account to the Court and that the same was subject to Court approval and therefore not due on the date of bankruptcy. Such is not the instant case where we have a vested contractual right of the bankrupt to share in the profits of the joint venture. The *Thomas* case is therefore not applicable.

Lockhart v. Mittleman, 123 F. 2d 703, C. C. A. Second (1939) cited in page 22 of the appellants' brief

may likewise be distinguished in that that case involved no fraud whatever, no fraudulent claim on the part of bankrupt to conceal assets from creditors, and like the *Thomas* case, *supra,* involves a State Court Trustee, the trustee's fee being subject to award of Court and no fee being due until an accounting by the Court was approved and is based upon that reason. That case is also a case on N. Y. State Law relating to State Court Trustees and it is respectfully submitted that the case has no applicability to the instant case nor is it analogous.

In re Coleman, 87 F. 2d 753, C. C. A. Second (1937), cited at page 23 of the appellants' brief, may likewise be distinguished in that that case involved a disbarred attorney who was entitled to no fees whatever until he had concluded a law suit. This was a contingent fee case and the decision was based upon the fact that under the State law the attorney would be entitled to nothing as he wrongfully terminated his employ by causing himself to be disbarred.

The Court stated that the significant feature is that there be a calculable value regardless of conditions. In the instant case, the bankrupt's rights under the contract of April 7, 1954 must certainly have had a calculable value and in view of the above distinguishing facts the Coleman case should have no applicability to the instant case, coupled with the fact that there was no scheme to hinder, delay, defraud or cheat the creditors of the bankrupt.

In the case of *Mersfelder v. Peters Cartridge,* 130 Ohio, C. C. N. S. 220, was a State Court decision in no way binding or persuasive authority regarding the Federal Bankruptcy Act.

It is respectfully submitted that in the instant case not only did the bankrupt fail to schedule any interest in the joint venture contract and any interest in the Pacific Palmdale Development Company, but commencing approximately nine months prior to bankruptcy engaged in a deliberate scheme to hinder, delay, defraud and cheat his creditors starting with the execution of an agreement to make his wife's property her separate property, culminating in the incorporation of a hollow shell of a corporation to channel his profits of a joint venture contract in such a manner as they would be insulated from creditors. In none of the cases cited by the appellants was there any such a deliberately devised scheme to hinder, delay, cheat and defraud creditors. While the appellee has been unable to locate any case authority to the effect that the bankrupt should be put to the burden of proof in a case of deliberate fraud, the appellee believes that this is a sound proposition and that the cases cited by the appellants have no applicability to a flagrant set of facts such as have been disclosed in the instant proceeding.

Conclusion.

We respectfully submit that the entire argument of the appellants is based on the mistaken assumption that Mr. Hudson was a mere employee and upon a distorted view of the facts which would have the Court believe that this is a simon-pure bankrupt who had no intention whatever of defrauding creditors and that even if he had had such intent, that creditors were not injured. On the contrary, at the time of bankruptcy, the Pacific Palmdale Development Company, being the alter ego of the bankrupt, the bankrupt had a vested interest in and to substantial profits which were realized and partially paid within approximately a month of his bankruptcy proceed-

ings. The Pacific Palmdale Development Company had no capital, no capital structure, and it is pointed out in the argument had no purpose save and except to hinder, delay and defraud the creditors of the bankrupt. The record is replete with evidence that the motivating factor behind the transaction was knowledge that the bankrupt was insolvent and that creditors could get at the interest of the bankrupt provided he accumulated any funds. At the very time of the execution of the agreements in this matter the bankrupt was preparing for bankruptcy and subsequently made no mention in his schedules of the entire affair.

It would indeed be a shocking travesty of justice if a bankrupt, such as the bankrupt in the instant case, could, without making any mention to the bankruptcy court, incorporate a corporation 13 days prior to bankruptcy, and enter into a joint venture, the result of which was to realize at least $44,000.00 to the bankrupt and yet have no portion of these moneys deliberately concealed from creditors, vulnerable to creditors. It would also be shocking if a bankrupt could, by delaying the acceptance of a contract until the very day of his bankruptcy, or the day afterwards, then be heard to argue that the profits realized were non-divisible and that by his own wrongful act, with Court sanction, he had placed his concealed funds beyond the reach of his creditors.

We therefore respectfully submit that no error has been shown on the part of this appellant and that the order of the District Court in this proceeding should be affirmed.

Respectfully submitted,

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